

2-24-10, Bernanke Warns Of Unsustainable Debt Path

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WASHINGTON -In response to questions from Financial Services Committee Ranking Member Spencer Bachus on whether federal deficit levels are unsustainable, Federal Reserve Chairman Ben Bernanke said that "given the numbers that the CBO or the OMB have projected, that's right." Federal Reserve Chairman Bernanke warned that "I do think that it's very important that we begin to look at the path, the trajectory, of the deficit as it goes forward." In response to a Bachus question on whether it was critical to have a long-term plan to reduce the debt, Bernanke said that "it would be very helpful, even to the current recovery, to market confidence, if there were a sustainable credible plan for a fiscal exit."

NOTE: Click [here](#) to view the video of the exchange. The transcript from today's House Financial Services Committee hearing follows:

BACHUS: Chairman Bernanke, Mr. Frank mentioned the deficit and the debt in passing. That's what I want to ask you about. Our debt is going to double in the next five years and triple in the next ten years. And it's fueled by historic deficits.

I heard this morning on TV that we have in many cases across the U.S. of children, and even adults, walking out on the thin ice. They walk out day after day and they get some comfort. But thin ice is dangerous. And, I submit that this type of budget path is dangerous and the deficit is dangerous. I would ask you, is our budget path sustainable, is there an urgent need for Congress to come up with a concrete plan to change that budget path, and do you believe there is an urgency in that?

BERNANKE: Congressman, when you ask about sustainability, you're talking about the medium-term structural deficit that remains even after the economy has returned close to more normal levels of activity.

Estimates of the structural deficit range from 4 percent by the OMB to up to 7 percent of GDP in some scenarios run by the CBO. Those numbers are above a sustainable level. I think in order to maintain a stable ratio of debt to GDP, you need to have a deficit that's 2.5 percent, 3 percent at the most.

So I think, yes, under current projections we have a deficit and a debt that will continue to grow. Interest rate costs that will continue to grow. So I do think that it's very important that we begin to look at the path, the trajectory, of the deficit as it goes forward. And there could be a bonus there. To the extent that we can achieve credible plans to reduce medium- to long-term deficits, we'll actually have more flexibility in the short term if we want to take other kinds of action.

BACHUS: Right. So the current budget path is not sustainable, is it?

BERNANKE: Given the numbers that the CBO or the OMB have projected, that's right.

BACHUS: And it might be upon us sooner than we think. Is that a good analogy that I've used, of walking on thin ice?

BERNANKE: Yes, sir, that's true. It's not necessarily just a long-term issue because it is possible that bond markets will become worried about the sustainability and we may find ourselves facing higher interest rates, even today, given that concern.

BACHUS: So is it critical that we have a long-term plan, and we have it now.

BERNANKE: Yes, I think it's very important that Congress -- I realize it's extremely difficult -- extremely difficult. I don't underestimate in any way how difficult it is. And it's also difficult to address issues which are still a few years away. I understand that as well.

But it would be very helpful, even to the current recovery, to market confidence, if there were a sustainable, credible plan for -- for a fiscal exit, if you will.

BACHUS: Well, if we don't address them now, I'm not sure we can address them, you know, in a effective way, two or three years from now or four or five years.

BERNANKE: It'll become increasingly difficult because the cuts that you'll need to make will be even sharper and with the tax increases, even sharper.

BACHUS: I very much appreciate your testimony. And I do believe that you've addressed many of the concerns. And I'm happy that you mentioned that this sterile reserves legislation [authorizing the payment of interest on excess reserves maintained at the Federal Reserve] that we passed in a bipartisan way has been an important tool.